

Order No. G04-54
Western Professional Insurance Company
Exhibit A

**WASHINGTON STATE
OFFICE OF THE INSURANCE COMMISSIONER**



FINANCIAL EXAMINATION
OF
WESTERN PROFESSIONAL INSURANCE COMPANY
SEATTLE
NAIC CODE 10942
EXAMINATION AS OF DECEMBER 31, 2001

Participating States:
Washington

CHIEF EXAMINER'S AFFIDAVIT

I hereby certify I have read the attached Report of the Financial Examination of WESTERN PROFESSIONAL INSURANCE COMPANY of Seattle, Washington. This report shows the financial condition and related corporate matters as of December 31, 2001.

A handwritten signature in black ink, reading "Patrick H. McNaughton". The signature is written in a cursive style with a large initial "P" and "M".

Patrick H. McNaughton, Chief Examiner

WESTERN PROFESSIONAL INSURANCE COMPANY
TABLE OF CONTENTS

SALUTATION	1
SCOPE OF EXAMINATION	1
INSTRUCTIONS	2
COMMENTS AND RECOMMENDATIONS	3
HISTORY	3
Capitalization and Dividends to Stockholders	
MANAGEMENT AND CONTROL	4
Board of Directors, Officers, Committees and Conflict of Interest Policy	
CORPORATE RECORDS	5
AFFILIATED INSURANCE COMPANIES	5
Organization Chart, Management Agreement, Tax Allocation Agreement, and Quota Share Reinsurance Agreement	
FIDELITY BOND AND OTHER INSURANCE	7
EMPLOYEES' BENEFIT PLANS	7
TERRITORY AND PLAN OF OPERATION	8
GROWTH OF COMPANY	8
ACTUARIAL REVIEW	8
REINSURANCE PROGRAM	8
INFORMATION SYSTEMS and ACCOUNTING RECORDS	9
SUBSEQUENT EVENTS	9
FINANCIAL STATEMENTS	9
NOTES AND COMMENTS TO FINANCIAL STATEMENTS	15
ACKNOWLEDGMENT	16
AFFIDAVIT	17

SALUTATION

Seattle, Washington
June 3, 2004

The Honorable Kevin McCarty
Director of Insurance Regulation
Florida Department of Financial Services
Chair, NAIC Financial Condition (E) Committee
200 E. Gaines Street, Room 101
Tallahassee, FL 32399-0301

The Honorable John Morrison
Commissioner, Montana Department of Insurance
Secretary, Western Zone
840 Helena Avenue
Helena, MT 59601

The Honorable Mike Kreidler
Commissioner, Washington State Office of the Insurance Commissioner (OIC)
PO Box 40255
Olympia, WA 98504-0255

Dear Commissioners:

In accordance with your instructions and in compliance with the statutes of the state of Washington, Chapter 48.03 Revised Code of Washington, an examination has been made of the corporate affairs and financial records of

WESTERN PROFESSIONAL INSURANCE COMPANY
of
Seattle, Washington

hereinafter referred to as the "Company" or "WPIC", at its home office located at 1730 Minor Avenue, Suite 1800, Seattle, Washington 98101. The following report on the examination is respectfully submitted showing the condition of the Company as of December 31, 2001.

SCOPE OF EXAMINATION

The first examination of the Company was a qualifying examination made as of July 31, 1998. The current examination conducted by insurance examiners from the state of Washington covered the period from August 1, 1998 through December 31, 2001. Additional examination procedures and testing were performed based upon subsequent events through April 30, 2003. The examination was conducted in accordance with the laws and regulations of the state of Washington contained in Title 48 of the Revised Code of Washington (RCW) and Title 284 of the Washington Administrative Code (WAC) and the examination procedures recommended by the National Association of Insurance Commissioners (NAIC) found in the NAIC Financial Condition Examiners Handbook.

Corporate records and various aspects of the Company's operating procedures and financial records were reviewed and tested during the course of this examination and are commented upon in the following sections of this report. The Company's certified public accountant's work papers were reviewed and utilized, where possible, to support efficiency in the examination.

INSTRUCTIONS

Pursuant to the findings and conclusions of the examiners and actuary, in accordance with sound actuarial principles, Title 48 RCW, Title 284 WAC and the NAIC Accounting Practices and Procedures Manual (APPM) for Property and Casualty Insurance Companies, the Company is hereby instructed to comply with the following:

1. Adhere to NAIC Annual Statement Instructions and the NAIC Accounting Practices and Procedures Manuals

The Master Custody Agreement does not contain a provision requiring "...the custodian to notify the Insurance Commissioner within three business days of termination or withdrawal of 100% of the account assets," pursuant to the guidelines in the NAIC Financial Examiners Handbook, Part 1, IV.H.2.f, Custodial Safekeeping Agreements.

Additionally, the Master Custody Agreement does not contain a provision requiring "...the custodian to secure and maintain insurance protection in an adequate amount pursuant to the guidelines in the NAIC Financial Condition Examiners Handbook, Part 1, IV.H.2.k, Custodial Safekeeping Agreements."

The Company is instructed to comply with WAC 284-07-050(2) which requires adherence to the appropriate Annual Statement Instructions and the APPM promulgated by the NAIC for the completion of the annual statement. This includes the 2001 NAIC Financial Condition Examiners Handbook.

2. Errors in Annual Statement

The corporate bylaws were amended in 2001. The General Interrogatory disclosure in the Company's Annual Statement was answered incorrectly as "NO" changes were made.

The Company is instructed to comply with RCW 48.05.250 which requires the Company to file with the Insurance Commissioner a true annual statement of its financial condition, transactions, and affairs.

3. Appointment of Committees

Article 3.13, Executive and Other Committees, of the bylaws says that the BOD, by resolution, may designate from among its members, an Executive Committee. The BOD may also, by resolution, designate other committees, consisting of other non-directors, but must contain at least one director.

An Investment Committee of the parent company routinely provides investment transaction reports to the WPIC BOD and the WPIC BOD routinely ratifies those reports. There are no WPIC BOD members on the PI Investment Committee. Three other committees of the parent company routinely report to the WPIC BOD. There is at least one WPIC board member on each of those committees.

The WPIC BOD has not noted, in any of its BOD meeting minutes compiled throughout the examination period, the designation of any committees by resolution or appointment of members to any committees.

The Company is instructed to comply with the terms of its bylaws and RCW 23B.08.010 and RCW 23B.080.250 of the Business Corporation Act and designate appropriate committees of the BOD by resolution and appoint members to those committees consisting of at least one member of the BOD. Actions and recommendations of the committees of the board should also be ratified and noted in the BOD meeting minutes.

COMMENTS AND RECOMMENDATIONS

Pursuant to the findings and conclusions of the examiners:

1. Conflict of Interest Disclosures

The Company's legal counsel performs the review of the annual conflict of interest disclosure statements completed by board of director members, company officers and others in key management positions and reports any potential conflicts to the BOD. The BOD meeting minutes do not contain any acknowledgment that the conflict of interest statements have been completed, reviewed, or that any potential conflicts were reported to the BOD.

It is recommended that the BOD include an acknowledgement in its meeting minutes that the conflict of interest statements have been completed by all appropriate persons and potential conflicts of interest were reported to the BOD.

HISTORY

Western Professional Insurance Company is a wholly owned subsidiary of Physicians Insurance A Mutual Company (Physicians Insurance, PI, or shareholder). WPIC was incorporated as a stock insurance company on May 8, 1998, and was granted a certificate of authority by the Washington State Office of the Insurance Commissioner (OIC) on October 22, 1998. WPIC provides comprehensive professional liability insurance to physicians and hospitals practicing in Washington, Oregon, and Montana, as well as business owner policies which cover insured's business property and provider excess insurance policies. WPIC also underwrites all of Physicians Insurance's non-professional liability insurance for physicians practicing in the state of Washington and began doing so on January 1, 1999. All business underwritten by WPIC is fully ceded to Physicians Insurance, except premiums related to the expense loading on facultative reinsurance.

Capitalization: The Company's articles of incorporation authorize the issuance of 1,000,000 shares \$10 par value common capital stock. Solicitation permit No. 284 authorized the raising of up to ten million dollars. Washington State Physicians Insurance Exchange (now Physicians Insurance A Mutual Company) subscribed to 300,000 shares for a total consideration of \$10,000,000. The solicitation permit was ultimately amended for the purpose of clarifying the division of the proceeds of the stock sale, \$3,000,000 being allocated to common capital stock and \$7,000,000 allocated to contributed surplus.

Dividends to Stockholders: Pursuant to RCW 48.31B.030(2)(a) and (b), without prior approval of the OIC, dividends to stockholders during the year 2001, were limited to the greater of ten percent (\$29,800) of the of the prior year surplus or net income (\$254,000) for the prior year, December 31, 2000. The Company did not declare or pay any dividends to stockholders during the examination period.

MANAGEMENT and CONTROL

Board of Directors: Control of the Company is vested in the BOD consisting of seven members as of December 31, 2001. An amendment to the bylaws of May 9, 2001 required the number of directors to be no less than seven (7) and no more than eleven (11) to assure that physician policyholders of the shareholder constitute a majority of the BOD. Positions one through four are non-physicians, and positions five through eleven are physician policyholders of the shareholder. BOD members are elected at the annual shareholders' meeting for a three-year term. Terms are staggered such that four persons could be elected in each of two consecutive years and three persons are elected every third year. Persons elected to the BOD may serve only nine (9) years during a lifetime. The Board of Directors on December 31, 2001 were as follows:

<u>Name and Address</u>	<u>Principal Business Affiliation</u>	<u>Member Since</u>
Gene Nels Peterson, MD	Medical Doctor	1998
Kazimer Byron Skubi, MD	Medical Doctor	1998
Rick Lane Johnson, MD	Medical Doctor	1998
James Paul Campbell, MD	Medical Doctor	1998
Dennis Ray Dahlin, MD	Medical Doctor	1998
Calvin Phillip Sandifer		1998
Lawrence Lee White, Jr.		1999

Officers: Officers are elected for a one-year term at the annual BOD meeting held immediately following the annual shareholder meeting. Officers on December 31, 2001 were:

<u>Name</u>	<u>Position held</u>
Thomas L. Myers	President and Chief Executive Officer
Richard E. Brown	Senior Vice President/Chief Financial Officer & Treasurer
Thomas A. Fine	Senior Vice President/Underwriting & Marketing
Bruce W. Schafer	Senior Vice President/Claims & Risk Management
Patricia C. Berger	Vice President/Litigation Management
Paul A. Buckner	Vice President/Eastern Regional Office
James J. J. Corbin	Vice President/Marketing
Terry B. Evans	Vice President/Information Services
John R. Karlen	Vice President/Products & Services Development
Thomas E. Kirchmeier	Vice President/Risk Management/Education
Judith J. Mix	Vice President/Corporate Secretary
Gary L. Morse	Vice President/General Counsel
Robert J. Nickles	Vice President/Oregon Regional Office
Vince A. Rota	Vice President/Hospitals
Pamela B. Tinsley	Vice President/Underwriting
Kristin L. Kenny	Associate Vice President/Controller

Committees: The bylaws provide for an Executive Committee and other standing committees. WPIC does not specifically designate committees of the BOD. However the designated committees of the parent company operate as combined committees with the affiliated companies. The Standing committees of the PI BOD are: Executive Committee; Audit Committee; Nominating Committee; Investment Committee; Underwriting/Marketing Committee; Claims Committee; and Risk Management/Education Committee. All committees of the parent met regularly, kept written records of their meetings and made regular reports to their respective company's BOD. Committee members were not regularly appointed. (See "INSTRUCTIONS" No. 3, Pg. 2.)

Conflict of Interest and Confidentiality Policy: The Company has a conflict of interest agreement and policy that requires the annual completion of a Conflict of Interest Agreement by officers, directors, and key employees. All are required to disclose to the corporate counsel relevant outside interests, memberships, associations, and affiliations. All appropriate persons have complied with this policy. Potential conflict of interest issues and confidential and proprietary information are provided to the BOD on a "need to know" basis as determined by the corporate counsel. There were no noted discussions in the BOD meeting minutes regarding the conflict of interest policy. It is recommended that the corporate counsel make an annual report to the BOD discussing relevant disclosures and noting that the disclosure process has been completed. (See "COMMENTS AND RECOMMENDATIONS" No. 1, Pg. 3.)

The examiners' review of the conflict of interest statement and confidentiality policy, and the Company's review process disclosed that the Company makes a concerted effort to protect the confidentiality of the Company strategy, all records, data and any other information of a private or sensitive nature and no conflicts have been disclosed.

CORPORATE RECORDS

The initial articles of incorporation were prepared in accordance with RCW 48.06.200, adopted by the Incorporators and filed with the Secretary of State of the state of Washington on May 8, 1998. There have been no amendments to the articles of incorporation.

The corporate bylaws were initially adopted by the BOD on June 16, 1998 and were restated on October 28, 1998. An amendment to Article 3.1 was adopted by the BOD on May 9, 2001 changing the number, tenure and qualifications of the BOD. The changes to the bylaws were not disclosed in the Annual Statement General Interrogatories. (See "INSTRUCTIONS" No. 2, Pg. 2.)

The BOD was active throughout the examination period. Meetings were well attended and the minutes were in sufficient detail and substance to demonstrate that the BOD members were actively involved in the administration of the affairs of the Company. All meetings were documented in written form, noting items of discussion and specific actions taken.

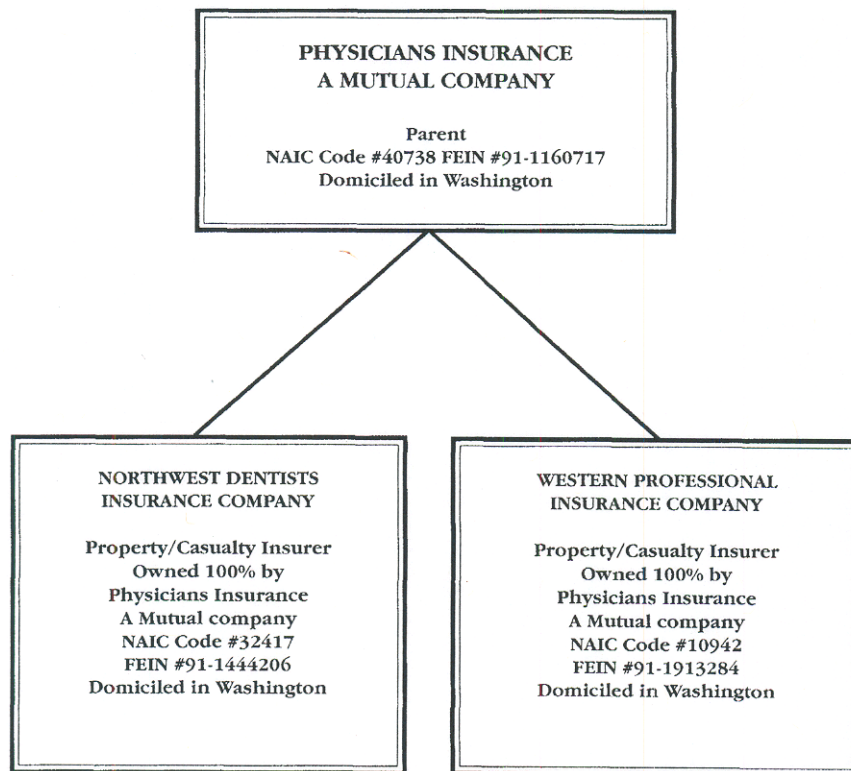
AFFILIATED INSURANCE COMPANIES

The following companies are all insurer members of a holding company group and have filed a registration statement under the provisions of Washington's Insurer Holding Company Act pursuant to Chapter 48.31B RCW. Annual Statement Instructions for Schedule Y, Part 2, do not require the disclosure of non-insurer affiliates, unless it is the parent company, or the transactions are equal to or greater than one-half of one percent of the total assets of the largest affiliated insurer. This reporting criteria is reflected in our examination report.

Physicians Insurance A Mutual Company (PI) is the reorganized company and it is commonly called by its registered trademark name of Physicians Insurance. PI provides comprehensive professional liability insurance to physicians practicing in Alaska, Idaho, Montana, Oregon and Washington.

Northwest Dentists Insurance Company (NORDIC) is a Washington corporation organized as a stock insurance company on May 10, 1989 by Physicians Insurance Exchange as its wholly owned subsidiary. The Company was organized to provide comprehensive professional liability insurance to dentists practicing principally in the state of Washington.

Organization Chart: The following organization chart depicts the relationship of the insurer affiliates under the COMPANY holding company system as of December 31, 2001.



The Company is a participant in several inter-company agreements. As a member of an insurance company holding system, these have been filed pursuant to RCW 48.31B.025 with the OIC. As of December 31, 2001, the Company was party to the following agreements:

Management Agreement: The Company entered into a Management Agreement with Washington State Physicians Insurance Association (WSPIA) on June 23, 1998, wherein WSPIA agreed to serve as the general manager for the insurance issued by the Company. The agreement outlines the duties and responsibilities of each party and reimbursement of fees for the services performed. These duties and responsibilities were assumed by Physicians Insurance A Mutual Company.

Tax Allocation Agreement: The Company files a consolidated federal income tax return with its parent, Physicians Insurance A Mutual Company, and the other affiliates. The method of allocation among the affiliated companies is subject to written agreement approved by the

Board of Directors. The agreement calls for allocation of taxes based upon separate return calculations with current credit for net losses. All amounts payable or receivable will be made by way of journal entries to inter-company accounts established for this purpose. Inter-company tax balances are settled annually in the first quarter.

On a consolidated basis, there was no taxable income in 2001.

FIDELITY BOND AND OTHER INSURANCE

The Company is a named insured on a Financial Institution Fidelity Bond. An aggregate loss limit of coverage in the amount of \$2,500,000 is provided for all of the affiliated companies insured and a single loss deductible is \$50,000. The minimum amount recommended by the NAIC for the three insurance companies is \$900,000 to \$1,000,000. The calculation indicates that the aggregate amount of coverage is adequate to cover the exposure risk of the Company and its affiliates.

The Company is also provided protection against certain property and liability losses as a named insured on several other policies.

Policies in effect at December 31, 2001 provided the following coverages:

- Directors and Officers Liability Insurance including Employment Practices Liability Coverage
- Commercial General Liability
- Commercial Umbrella Liability Policy

The Company does not have any "Errors and Omissions" coverage. The Company has chosen to be self insured for this hazard and risk.

The review of the Company's insurance policies indicated that adequate insurance coverage has been purchased and is in force covering the hazards to which the Company is exposed as of the examination date.

EMPLOYEES' BENEFIT PLANS

Physicians Insurance A Mutual Company is the employer for all affiliated companies. Salaries and benefits are allocated to the three affiliated insurance companies based upon management and allocation agreements: 75% to PI, 15% to WPIC and 10% to NORDIC.

Employees who are twenty-one years old and have completed one month of service are eligible to participate in two defined contribution plans. For 401(k) participants, employees may make pre-tax contributions up to 8% of their base compensation per year, to which the Company will match these contributions up to 6.6% of the employees' base compensation. The Company currently contributes 10% of the employees' base compensation to the Money Purchase Plan and employees may make voluntary after-tax contributions to the plan.

Vesting requirements are five years of service for 100% of the employer's contribution and immediate vesting for 100% of the employee's contribution.

The Company also provides other plans and benefits to its employees such as Medical and Dental Insurance, Life Insurance and Accidental Death and Dismemberment Insurance, Long-Term Disability, Travel Accident Insurance, Employee Assistance Program (EAP), Workers'

Compensation Insurance, Education and Course Reimbursement. The Company also offers the usual options for time off from work including vacation, holidays, sick leave and other leaves of absence.

TERRITORY AND PLAN OF OPERATION

Western Professional Insurance Company was granted a certificate of authority in the state of Washington on October 22, 1998 which authorized the Company to provide comprehensive professional liability insurance to physicians and hospitals practicing in the state of Washington as well as business owner policies which cover insureds' business office property. WPIC is also licensed in the states of Idaho (as of June 15, 2001), Montana (as of February 24, 2000) and Oregon (as of January 10, 2000).

GROWTH OF COMPANY

The following are the Company's historical direct writings:

Direct Premiums Written by State (Schedule T – Premiums)

	<u>1999</u>	<u>2000</u>	<u>2001</u>
Washington	\$11,014,463	\$11,365,882	\$10,373,670
Oregon		391,755	2,279,014
Montana		1,407,061	1,726,243
Idaho			8,687
	<u>\$11,014,463</u>	<u>\$13,164,698</u>	<u>\$14,387,614</u>

Direct Premiums Written by Line of Business

	<u>1999</u>	<u>2000</u>	<u>2001</u>
Commercial Multiple Peril	\$383,763	\$412,119	\$420,796
Medical Malpractice	4,786,470	6,934,416	8,506,826
Other Liability	223,177	2,699	1,700
Provider Excess Liability	5,621,053	5,815,464	5,458,292
	<u>\$11,014,463</u>	<u>\$13,164,698</u>	<u>\$14,387,614</u>

ACTUARIAL REVIEW

The Company cedes all of its losses, except for facultative reinsurance contracts with other companies for limits above \$5 million, and almost all of its loss adjustment expenses to Physicians Insurance A Mutual Company pursuant to a 100% quota share reinsurance agreement. The one-year and two-year loss development figures on page 23 of the 2001 and 2002 Annual Statements are all zeros. Unallocated loss adjustment expense on medical malpractice coverage is retained by the Company and unallocated loss adjustment expense on other than medical malpractice coverage is ceded. Ceded losses and loss adjustment expenses were reviewed as part of the OIC actuarial review of PI. WPIC reserves are accepted as shown in the 2001 Annual Statement.

REINSURANCE PROGRAM

The Company is part of a Quota Share Reinsurance Agreement with its parent, Physicians Insurance A Mutual Company, covering all lines of business. The agreement applies to 100% of the Company's premium on business covered which is ceded to the parent up to policy limits of \$5,000,000. Higher limits are placed in the facultative market. The reinsurer parent is liable

for 100% of the losses and allocated loss adjustment expenses with respect to the business covered.

INFORMATION SYSTEMS AND ACCOUNTING RECORDS

The management of Physicians Insurance, as provider of information systems technology and services to WPIC, is sufficiently knowledgeable of EDP issues and provides direction and oversight through its Steering Committee. New systems development, acquisition and maintenance controls have been reviewed to gain assurance that programs and systems are designed, tested, approved and implemented using appropriate controls. The internal controls in place provide for the proper separation of duties.

Operations controls and application controls were reviewed to determine the type of hardware installed; operating systems and proprietary software in use; back up and recovery facilities employed and the controls exercised to maintain data security. Adequate procedures and controls are in place for mainframe and network operations.

SUBSEQUENT EVENTS

Subsequent to the examination date, a moratorium on new business was declared by management in the fall of 2002. Market share has declined slightly in 2003 as a result of the moratorium.

Since the examination date, Thomas A. Fine, Senior Vice President/Underwriting & Marketing and Patricia Claire Berger, Vice President/Litigation Management, retired, and Thomas L. Myers, President and Chief Executive Officer announced his retirement.

FINANCIAL STATEMENTS

The following statements reflect the financial condition of the Company as of December 31, 2001, as determined by this examination:

Balance Sheet
As of December 31, 2001

Comparative Balance Sheet
Years Ended December 31, 2000 and 2001

Statement of Income
As of December 31, 2001

Comparative Statement of Income
Years Ended December 31, 2000 and 2001

Capital and Surplus Account
As of December 31, 2001

Comparative Capital and Surplus Account
Years Ended December 31, 2000 and 2001

WESTERN PROFESSIONAL INSURANCE COMPANY
BALANCE SHEET
AS OF DECEMBER 31, 2001

	<u>BALANCE PER COMPANY</u>	<u>EXAMINATION ADJUSTMENTS</u>	<u>BALANCE PER EXAMINATION</u>	<u>Notes</u>
<u>ASSETS</u>				
Bonds	\$9,368,496		\$9,368,496	1
Cash and short-term investments	2,470,596		2,470,596	2
Agents' balances or uncollected premiums:				
Premiums in course of collection	2,004,566		2,004,566	
Reinsurance recoverable	696,270		696,270	
Federal income tax recoverable	1,699		1,699	3
Interest and dividend income due and accrued	131,742		131,742	
	<u>\$14,673,369</u>	<u>\$0</u>	<u>\$14,673,369</u>	
Total assets				
<u>LIABILITIES</u>				
Loss adjustment expenses	200,000		200,000	4
Other expenses (excluding taxes, licenses & fees)	74,110		74,110	
Taxes, licenses & fees (excl. fed. inc. tax)	24,109		24,109	
Fed. and foreign inc. taxes (excl. def. taxes)	113,312		113,312	
Ceded reinsurance premiums payable	3,037,355		3,037,355	
Payable to parent, subsidiaries and affiliates	557,063		557,063	
Aggregate write-ins for liabilities	194,914		194,914	5
	<u>4,200,863</u>	<u>0</u>	<u>4,200,863</u>	
Total liabilities				
<u>SURPLUS AND OTHER FUNDS</u>				
Common capital stock	3,000,000		3,000,000	
Gross paid in and contributed surplus	7,000,000		7,000,000	
Unassigned funds (surplus)	472,506		472,506	
	<u>10,472,506</u>	<u>0</u>	<u>10,472,506</u>	
Surplus as regards policyholders				
Total liabilities, surplus and other funds	<u>\$14,673,369</u>	<u>\$0</u>	<u>\$14,673,369</u>	

WESTERN PROFESSIONAL INSURANCE COMPANY

COMPARATIVE BALANCE SHEET

AS OF DECEMBER 31,

	<u>2001</u>	<u>2000</u>
<u>ASSETS</u>		
Bonds	\$9,368,496	\$9,604,266
Cash and short-term investments	2,470,596	2,362,898
Agents' balances or uncollected premiums:		
Premiums in course of collection	2,004,566	1,260,477
Reinsurance recoverable	696,270	518,415
Federal income tax recoverable	1,699	
Interest and dividend income due and accrued	131,742	151,070
Total assets	<u>\$14,673,369</u>	<u>\$13,897,126</u>
<u>LIABILITIES</u>		
Loss adjustment expenses	200,000	200,000
Other expenses (excluding taxes, licenses & fees)	74,110	40,279
Taxes, licenses & fees (excl. fed. inc. tax)	24,109	54,015
Fed. and foreign inc. taxes (excl. def. taxes)	113,312	134,805
Ceded reinsurance premiums payable	3,037,355	2,327,180
Payable to parent, subsidiaries and affiliates	557,063	564,707
Payable for securities		97,795
Aggregate write-ins for liabilities	194,914	179,897
Total liabilities	<u>4,200,863</u>	<u>3,598,678</u>
<u>SURPLUS AND OTHER FUNDS</u>		
Common capital stock	3,000,000	3,000,000
Gross paid in and contributed surplus	7,000,000	7,000,000
Unassigned funds (surplus)	472,506	298,448
Surplus as regards policyholders	<u>10,472,506</u>	<u>10,298,448</u>
Total liabilities, surplus and other funds	<u>\$14,673,369</u>	<u>\$13,897,126</u>

WESTERN PROFESSIONAL INSURANCE COMPANY

STATEMENT OF INCOME YEAR ENDED DECEMBER 31, 2001

	<u>BALANCE PER COMPANY</u>	<u>EXAMINATION ADJUSTMENTS</u>	<u>BALANCE PER EXAMINATION</u>
<u>UNDERWRITING INCOME</u>			
Premiums earned	\$32,470	\$0	\$32,470
DEDUCTIONS:			
Loss expenses incurred	206,573		206,573
Other underwriting expenses incurred	204,719		204,719
Total underwriting deductions	411,292	0	411,292
Net underwriting gain or (loss)	(378,822)	0	(378,822)
<u>INVESTMENT INCOME</u>			
Net investment income earned	589,807		589,807
Net realized capital gains or (losses)	88,836		88,836
Net investment income gain or (loss)	678,643	0	678,643
<u>OTHER INCOME</u>			
Net gain or loss			
from agents' or premium balances charged off	(417)		(417)
Finance and service charges			
not included in premiums	8,174		8,174
Total other income	7,757	0	7,757
Net income before dividends to policyholders and before federal and foreign income taxes	307,578	0	307,578
Net income before federal and foreign income taxes	307,578	0	307,578
Federal and foreign income taxes incurred	113,357		113,357
Net income	\$194,221	\$0	\$194,221

WESTERN PROFESSIONAL INSURANCE COMPANY
COMPARATIVE STATEMENT OF INCOME
FOR THE YEARS ENDED DECEMBER 31,

	<u>2001</u>	<u>2000</u>
<u>UNDERWRITING INCOME</u>		
Premiums earned	<u>\$32,470</u>	<u>\$53,673</u>
DEDUCTIONS:		
Loss expenses incurred	206,573	142,579
Other underwriting expenses incurred	<u>204,719</u>	<u>137,279</u>
Total underwriting deductions	<u>411,292</u>	<u>279,858</u>
Net underwriting gain or (loss)	<u>(378,822)</u>	<u>(226,185)</u>
<u>INVESTMENT INCOME</u>		
Net investment income earned	589,807	607,304
Net realized capital gains or (losses)	<u>88,836</u>	<u></u>
Net investment income gain or (loss)	<u>678,643</u>	<u>607,304</u>
<u>OTHER INCOME</u>		
Net gain or loss		
from agents' or premium balances charged off	(417)	1,255
Finance and service charges		
not included in premiums	<u>8,174</u>	<u>6,418</u>
Total other income	<u>7,757</u>	<u>7,673</u>
Net income before dividends to policyholders and before federal and foreign income taxes	<u>307,578</u>	<u>388,792</u>
Net income before federal and foreign income taxes	307,578	388,792
Federal and foreign income taxes incurred	<u>113,357</u>	<u>134,805</u>
Net income	<u>\$194,221</u>	<u>\$253,987</u>

WESTERN PROFESSIONAL INSURANCE COMPANY

CAPITAL AND SURPLUS ACCOUNT

AS OF DECEMBER 31, 2001

	<u>BALANCE PER COMPANY</u>	<u>EXAMINATION ADJUSTMENTS</u>	<u>BALANCE PER EXAMINATION</u>
Surplus as regards policyholders, December 31, previous year	<u>\$10,298,449</u>	<u>\$0</u>	<u>\$10,298,449</u>
<u>GAINS AND (LOSSES) IN SURPLUS</u>			
Net income	194,221		194,221
Change in non-admitted assets	(21,863)		(21,863)
Cumulative effect of change in accounting principles	<u>1,699</u>		<u>1,699</u>
Changes in surplus	<u>174,057</u>	<u>0</u>	<u>174,057</u>
Surplus as regards policyholders, December 31, current year	<u><u>\$10,472,506</u></u>	<u><u>\$0</u></u>	<u><u>\$10,472,506</u></u>

COMPARATIVE CAPITAL AND SURPLUS ACCOUNT

AS OF DECEMBER 31,

	<u>2001</u>	<u>2000</u>	<u>1999</u>	<u>1998</u>
Surplus as regards policyholders, December 31, previous year	<u>\$10,298,449</u>	<u>\$10,068,270</u>	<u>\$10,198,090</u>	
<u>GAINS AND (LOSSES) IN SURPLUS</u>				
Net income	194,221	253,987	(129,820)	198,090
Change in non-admitted assets	(21,863)	(23,808)		
Cumulative effect of change in accounting principles	1,699			
Capital changes				3,000,000
Surplus adjustments				<u>7,000,000</u>
Changes in surplus	<u>174,057</u>	<u>230,179</u>	<u>(129,820)</u>	<u>10,198,090</u>
Surplus as regards policyholders, December 31, current year	<u><u>\$10,472,506</u></u>	<u><u>\$10,298,449</u></u>	<u><u>\$10,068,270</u></u>	<u><u>\$10,198,090</u></u>

NOTES AND COMMENTS TO FINANCIAL STATEMENTS

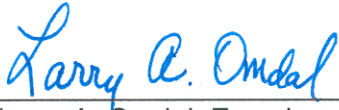
1. **BONDS** in the amount of \$9.37 million represent 63.8% of total assets; a decrease of 21% from the year 1999. Bonds are stated at amortized cost, secured, and not in default as to principle and interest. The Company accrues discounts and amortizes premiums using the scientific method. Mortgage-backed securities are adjusted using the prospective method.
2. **CASH AND SHORT TERM INVESTMENTS** are \$2.47 million and 16.8% of total assets. Short term investments with maturity dates of one year or less, consisted of two NAIC Class 1 money market mutual funds valued at \$860,000. Cash items consisted primarily of demand deposits.
3. **FEDERAL INCOME TAX RECOVERABLE** is \$1,699. The Company files a consolidated return with its parent Physicians Insurance A Mutual Company and affiliates. The method of allocation among the companies is subject to written agreement approved by the Board of Directors. Allocation is based upon separate return calculations with current credit for net losses. Inter-company balances are settled annually in the first quarter of the following year.
4. **LOSSES AND LOSS ADJUSTMENT EXPENSES** are immaterial. The Company has retained unallocated loss adjustment expense on medical malpractice coverage which is reflected in the estimated loss adjustment expenses reserve as of December 31, 2001.
5. **AGGREGATE WRITE-INS FOR LIABILITIES** are \$194,914 or 1.39% of total assets. The total amount represents premiums received in advance. The premium accounting system tracks premiums received in advance and nets them against premiums receivable. The Company makes a reclassification entry from premiums receivable to aggregate write-ins in order to not distort actual premiums receivable.

ACKNOWLEDGMENT

Acknowledgement is hereby made of the cooperation extended to the examiners by the officers and employees of Western Professional Insurance Company during the course of this examination.

In addition to the undersigned, Constantine Arustamian, CPA, Insurance Examiner, Friday Enoye, Insurance Examiner, Juanita Turley, Insurance Examiner, John Gaynard, AFE, CPA, CPCU, Insurance Examiner and Reinsurance Specialist, John Jacobson, AFE, Insurance Examiner/Field Supervisor and EDP Specialist, Lee Barclay, FCAS, MAAA, ARM, Senior Actuary and Jim Antush, Actuarial Analyst, all from the OIC, participated in the examination and preparation of this report.

Respectfully submitted,



Larry A. Omdal, Examiner in Charge
State of Washington

AFFIDAVIT

State of Washington)
) ss
County of King)

Larry A. Omdal, being duly sworn, deposes and says that the foregoing report subscribed by him is true to the best of his knowledge and belief.

He attests that the examination of Western Professional Insurance Company was performed in a manner consistent with the standards and procedures required or prescribed by the Washington State Office of the Insurance Commissioner and the National Association of Insurance Commissioners.

Larry A. Omdal
Larry A. Omdal, Examiner in Charge
State of Washington

Subscribed and sworn to before me on this 3rd day of June, 2004.

Colleen Jansen
Notary Public in and for the
State of Washington, residing at Seattle.

